PSPP

# Public Service Pension Plan (Alberta)

# 1994

## Annual Report

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## PROFILE

- The Public Service Pension Plan was established April 1, 1947, to provide a contributory defined benefit pension scheme for the employees of the Government of Alberta, its agencies, boards, commissions, and other public bodies approved by the Lieutenant Governor in Council.
- A six-member pension board governs the Plan and is comprised of three employee representatives nominated by the Alberta Union of Provincial Employees and three employer representatives nominated by the Government of Alberta.
- The Plan is administered on behalf of 46 participating employers, approximately 45,000 active members and 13,000 pensioners.
- Employee and employer contributions and the investment earnings of the plan fund finance the benefits. In addition to making current service contributions as employer, the Government of Alberta shares in the funding of service accumulated before 1992.
- Plan investments total approximately $2.2 billion and comprise a diversified portfolio of equities (both domestic and international), money market securities, bonds, mortgages and real estate. Investment policy guidelines are set by the Board and the portfolio is managed by the Investment Management Division (IMD) of Alberta Treasury.

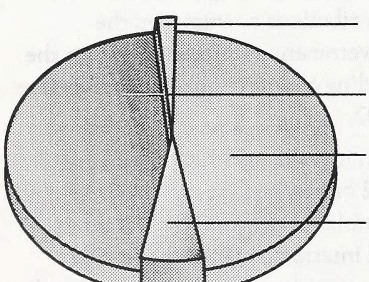
# FINANCIAL HIGHLIGHTS

AS AT DECEMBER 31, 1994

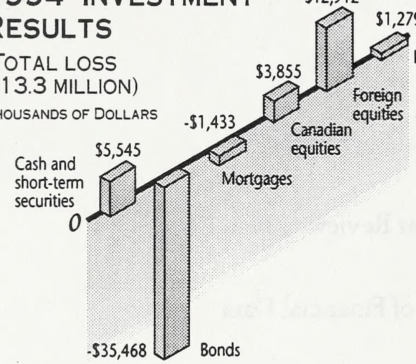
The following table summarizes the actuarial value of assets, the estimated cost of benefits, and the resulting actuarial deficiency at December 31, 1994:

| | ($ millions) |
|---|---|
| Cash and short-term securities | 223.7 |
| Bonds | 909.2 |
| Mortgages | 64.0 |
| Canadian equities | 500.0 |
| Foreign equities | 431.3 |
| Real estate | 55.3 |
| Other net assets | 28.9 |
| Total net assets | 2,212.4 |
| Actuarial asset value adjustment | 62.8 |
| Actuarial value of assets | 2,149.6 |
| Estimated cost of benefits | 2,768.0 |
| Deficiency | 618.4 |

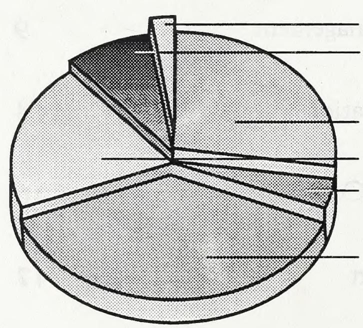
## 1994 CONTRIBUTIONS
(TOTAL $157.1 MILLION)



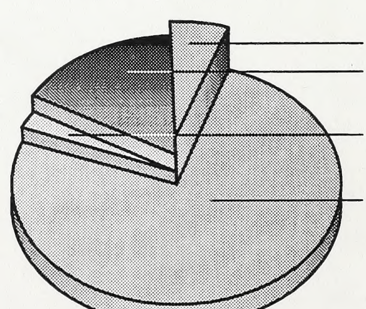

## 1994 INVESTMENT RESULTS
(TOTAL LOSS $13.3 MILLION)
THOUSANDS OF DOLLARS




## 1994 INVESTMENT ASSET MIX AT MARKET VALUE
(TOTAL $2,183.5 MILLION)




## 1994 PAYMENTS
(TOTAL $159.0 MILLION)



## FIVE-YEAR REVIEW OF PLAN DATA

| Plan Data | 1994 | 1993 | 1992 | 1991 | 1990 |
|---|---|---|---|---|---|
| **Number of employers** | 46 | 46 | 48 | 48 | 47 |
| **Number of active members** | 44,981 | 47,882 | 51,203 | 51,804 | 50,940 |
| **Number of pensions granted by type of pension** | | | | | |
| Normal retirement | 131 | 200 | 203 | 152 | 152 |
| Early retirement | 857 | 603 | 440 | 280 | 241 |
| Disability retirement | 14 | 4 | 8 | 8 | 9 |
| Death-in-service (spousal) retirement | 35 | 37 | 33 | 33 | 28 |
| **Total membership comprising active members, inactive members and pensioners** | 60,926 | 63,176 | 65,487 | 65,778 | 64,862 |

## REVIEW OF FINANCIAL DATA

| Financial Data ($ thousands) | Year Ended December 31, 1994 | Three Months Ended December 31, 1993 |
|---|---|---|
| **Assets** | 2,212,423 | 2,227,001 |
| **Investment (loss) income** | (13,310) | 111,149 |
| **Contributions – post-1991 service** | | |
| Employer | 66,564 | 17,942 |
| Employee | 70,321 | 18,890 |
| Transfers from other plans | 1,313 | 470 |
| **Contributions – pre-1992 service** | | |
| Employer | 3,545 | 787 |
| Employee | 3,545 | 787 |
| Government of Alberta | 11,818 | 2,625 |
| **Benefit payments and transfers** | | |
| Pensions | 115,472 | 28,100 |
| Refunds | 32,601 | 4,525 |
| Transfers to other plans | 7,878 | 1,353 |
| **Administration expenses** | | |
| Plan administration | 2,735 | 759 |
| Investment management | 315 | 55 |

Note: A separate pension fund for the Public Service Pension Plan was established on September 30, 1993 and received an allocation of assets held in the old Pension Fund.

# EMPLOYER LISTING

## AS AT DECEMBER 31, 1994

Agriculture Financial Services Corporation
Alberta Agricultural Development Corporation
Alberta Cancer Board
Alberta East Central Health Unit
Alberta Educational Communications Corporation
Alberta Liquor Control Board
Alberta Opportunity Company
Alberta Petroleum Marketing Commission
Alberta Racing Commission
Alberta Special Waste Management Corporation
Alberta Treasury Branches
Alberta Union of Provincial Employees
Alberta West Central Health Unit
Athabasca Health Unit
Athabasca University
Banff National Park Health Unit
Barons-Eureka-Warner Health Unit
Big Country Health Unit
Chinook Health Unit
City of Lethbridge Health Unit
Drumheller Health Unit
Energy Resources Conservation Board
Foothills Health Unit
Fort McMurray and District Health Unit
Government of Alberta
High Level-Fort Vermilion Health Unit
Jasper National Park Health Unit
Leduc-Strathcona Health Unit
Minburn-Vermilion Health Unit
Mount View Health Unit
North Eastern Alberta Health Unit
Peace River Health Unit No. 21
Red Deer Regional Health Unit
South Peace Health Unit
Southeastern Alberta Health Unit
Special Areas Board
Stony Plain-Lac Ste. Anne Health Unit
Sturgeon Health Unit
The Banff Centre
The University of Calgary
University of Alberta
University of Alberta Hospitals
University of Lethbridge
Vegreville Health Unit
Wetoka Health Unit
Workers' Compensation Board

# COMMENTS FROM THE BOARD

The Public Service Pension Plan Act, passed in 1993, and subsequent regulations under that Act have significantly changed the Public Service Pension Plan. The changes result from two years of discussion involving members, employers, the previous Board and the Government of Alberta.

The main reason for change was the need to put the Plan on a sound financial footing. In particular, there was a need to develop a plan to eliminate the unfunded liability related to service before 1992. It was also necessary to lay the groundwork for the eventual transfer of governance of the Plan to a representative Board of Trustees, thereby ensuring accountability to members.

Some of the key changes were:

- Appointing a new six-member Board
- Establishing a pension fund with assets in excess of $2.1 billion
- Paying a market rate of interest (1994: 6.7%) on refunded contributions, effective 1994
- Paying vested members who terminate a commuted value benefit for service after 1991
- Guaranteeing annual cost-of-living adjustments to pensions of at least 60% of inflation
- Requiring additional contributions from employers, members and the government to eliminate, by the year 2036, the unfunded liability related to service before 1992
- Charging members who buy optional service the full actuarial cost.

The Lieutenant Governor in Council appointed members to the new Pension Board in December 1993. The Board's responsibilities are:

- To set policy guidelines for investing the fund's assets and administering the Plan
- To set contribution rates that will fully fund current service and eliminate the unfunded liability related to service before 1992
- To make recommendations for future amendments to pension plan rules and provisions
- To conduct an actuarial valuation of the Plan at least every three years
- To ensure the Plan is administered effectively
- To review decisions made by the Administration.

The Board immediately started to address its new responsibilities.

Before September 30, 1993, the assets of six Alberta public sector pension plans, including the Public Service Pension Plan, were combined in one fund. These combined assets were split between the various plans on September 30, 1993. The Public Service Pension Plan Fund received its share amounting to $2,109 million. The value of the fund had increased to $2,227 million by December 31, 1993, because investment earnings and contributions flowing into the fund exceeded benefit payments and other costs for the period.

The plan fund received contributions of $157.1 million during 1994 along with $0.6 million of interest paid by the Government of Alberta. Pension benefit costs for the period were $155.9 million, administration costs were $3.1 million, and there was an investment loss of $13.3 million. Therefore, net assets for the period decreased by $14.6 million, resulting in a fund value of $2,212 million at the end of 1994.

The Board identified the setting of investment policy guidelines for the fund's assets as its most critical early priority. The Board agreed to a *Statement of Investment Policies and Goals* setting out general guidelines to be used by Treasury's Investment Management Division (IMD) when managing the fund's assets. The Board also hired an investment asset consultant, Frank Russell Canada Ltd. The consultant will help the Board to develop a long-term investment policy and a strategy for performance measurement.

Generally unfavourable investment market conditions in 1994 resulted in a zero rate of return on the overall asset portfolio. However, this return exceeded the median return achieved by other balanced fund managers which was a negative 0.7%. The average rate of return over the last four years was 10.6%, or 8.6% after subtracting inflation. This return substantially exceeded the assumed real rates of return of 3.5% and 4% in the 1991 and 1993 actuarial valuations. These investment results are explained further in the Investment Management section of this report, beginning on page 9.

Another Board priority during 1994 was to examine contribution rates and assess the Plan's current funding status. In August, the Board increased contribution rates for both members and employers in accordance with the schedule agreed between the previous Board and the government. The rates increased to 4.675% on salary up to the Year's Maximum Pensionable Earnings (YMPE) under Canada Pension Plan and 6.55% on salary over the YMPE.

Both members and employers pay additional contributions at the rate of 0.3% of total salary toward eliminating the unfunded liability by December 31, 2036. The Government of Alberta contributes 1.0% of total salary.

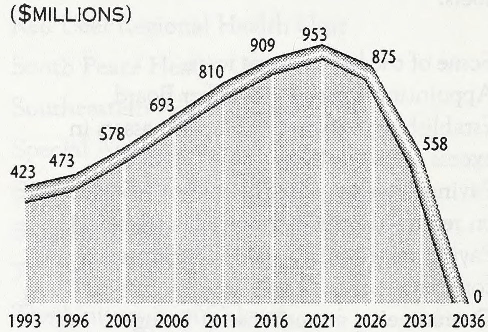
The Board hired Buck Consultants to act as actuarial consultants to the Plan. The firm conducted an actuarial valuation at December 31, 1993, to determine the current financial status of the Plan and to make sure contribution rates were sufficient to fund the benefits promised to members.

The valuation showed an actuarial liability of $2,568 million for pension benefits accrued to December 1993, compared with assets having an actuarial value of $2,047 million. The resulting unfunded liability was $521 million.

The valuation also disclosed that the expected normal cost of current service benefits expected to be earned in 1994 was 9.8% of pensionable earnings and that additional contributions of 1.6% would eliminate the unfunded liability by the year 2036. The graph below illustrates, on a funding basis, the actuary's projection of the growth and subsequent elimination of the unfunded liability.

## Pre-1992 Unfunded Liability

($MILLIONS)




Based on these findings, the Board decided no further change was required to current or additional contribution rates. The Board will set future contributions rates based on the findings of future actuarial valuations.

Using the December 1993 valuation as a base, the actuary projected the liability for accrued pension benefits to December 31, 1994. Considering the actuarial value of assets at the end of 1994, the result was an increase in the unfunded liability from $521 million to $618 million during 1994. The Board does not expect that this poor one-year investment performance will harm the Plan's long-term funding position.

One of the Board's highest priorities was to establish ongoing and effective communication with members and employers. To meet this goal, the Board initiated several communication projects during 1994.

We issued newsletters in June and September informing members of the Board's activities and outlining key issues affecting the Plan. Further newsletters are planned.

A completely redesigned member handbook was distributed in November. The handbook provides members with an easy-to-read summary of Plan rules and provisions.

As part of its responsibility to ensure the Plan is administered effectively, the Board reviewed 1994 and 1995 administration cost budgets prepared by Alberta Pensions Administration (APA). The review covered both general administration and investment costs, and looked at performance measures for both of these areas.

Based on total administration costs of $3.05 million for 1994, the average cost per member was $49. General administration costs, excluding investment management, were $44 per member. To assess the reasonableness of these costs, APA participated in a cost comparison survey with other pension plans across Canada. The survey results showed that APA costs compare favourably with other large public sector pension plans.

Investment management costs incurred by Treasury's Investment Management Division amounted to 1.43 basis points of total assets managed for the Plan. These costs also compare favourably to other similar investment operations.

The Board viewed reorganization in the health care sector as an important issue during 1994. We asked the Provincial Treasurer to establish a task force, including representatives of the Public Service Pension Plan, the Local Authorities Pension Plan, the Government and health sector representatives, to look at how pension plan members will be affected by the reorganization.

We have had a challenging and productive year. As Board members, we developed insight into many complex financing, investment and pension issues affecting the Plan. We also tried to represent the interests of Plan members by ensuring the financial health of the Plan. Major challenges for 1995 will be to finalize investment policy guidelines, to assess how the Plan will be affected by public sector restructuring, and to continue to develop an effective communication program with stakeholders.

Finally, we would like to thank the Provincial Treasurer, the staff of Alberta Pensions Administration and the Investment Management Division of Alberta Treasury for their help in managing the plan.

Approved on behalf of the Board:

Debbie Horbach (Chair)
Tim Wiles (Vice-Chair)
Gladys Breckenridge
Len Pederson
Don Windsor
Terry Burns (to December, 1994)
Al Kalke (from February, 1995)

# INVESTMENT MANAGEMENT

## Investment Policy

Under the Plan's interim investment policy, our objective for the fund is to earn the best possible rate of return consistent with an acceptable level of risk. In this way, we can avoid increases in contribution rates and ensure that members receive the retirement benefits promised to them. This investment policy is formally expressed in the document *Statement of Investment Policies and Goals* which is reviewed and updated at least annually by the Board.

Investment Management Division (IMD) controls and directs the fund's day-to-day investment operations ensuring that investment transactions are executed properly and that all securities and certificates are received, accounted for and kept in safe custody. We also provide the Board with recommendations and background material on investments, keep them informed of investment costs and report investment activities and results on a quarterly basis.

IMD is complemented by a team of external managers who enhance the diversity of the fund and provide specialized knowledge. These external managers directly manage assets and also provide additional market information. About 18% of the fund is managed externally under the supervision of IMD.

We have adopted a diversified approach to managing the fund's investment portfolio. This allows us to meet the challenges of a complex market environment in which different asset classes, such as bonds and equities, have different characteristics in terms of return and volatility.

Equities (corporate shares) have historically produced the highest long-term returns but often suffer from dramatic swings in year-to-year returns and generate most of their return through capital appreciation. Bonds are generally more secure and, if held to maturity, show consistent income cash flows. Studies show that an investment portfolio incorporating a mix of different types of investments is likely to successfully manage the risks faced by a fund and should keep that fund in a sound financial position over the long term.

The Public Service Pension Plan Fund faces numerous risks and difficulties. The Plan provides pensions indexed at 60% of inflation. This means the fund should hold equity assets that will perform well in inflationary periods.

The Plan is maturing and benefit payments are starting to exceed new contributions. The fund should also hold assets such as bonds and mortgages that generate regular, secure income to the fund.

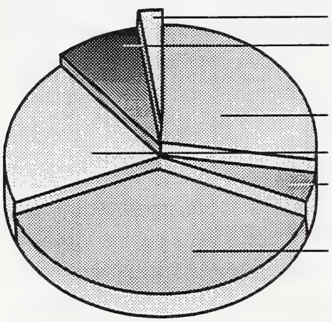
The following table shows the broad categories of investments held at December 31, 1994, their proportion of total investments, and the allowable percentage range for each investment category which would allow IMD to meet the previously outlined challenges.

### ASSET MIX (MARKET VALUE) AS AT DECEMBER 31, 1994

| | $ Millions | Actual % | Policy % |
|---|---|---|---|
| Cash & short-term securities | 224 | 10.3 | 0-20 |
| Bonds | 909 | 41.6 | 30-55 |
| Mortgages | 64 | 2.9 | 0-10 |
| Total fixed income | 1,197 | 54.8 | 35-65 |
| Equities – Canadian | 500 | 22.9 | 20-56 |
| – foreign | 431 | 19.8 | 10-24 |
| Real estate | 55 | 2.5 | 0- 8 |
| Total equity and real estate | 986 | 45.2 | 35-65 |
| TOTAL | 2,183 | 100.0 | |

## Investment Policy (continued)

### Asset Mix
(Total $2,183.5 million)

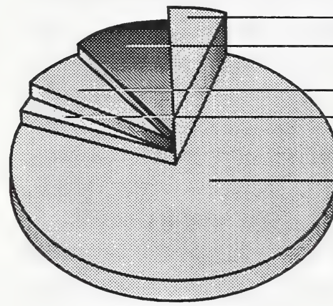



The Plan's interim investment policy allows IMD to adjust the fund asset mix when necessary.

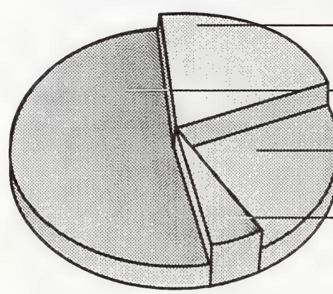
IMD has set a specific investment performance objective designed to ensure that the fund achieves a competitive market rate of return within investment policy constraints. The objective is to attain second quartile performance for the total fund as measured by a qualified independent measurement service over a rolling four-year period. A four-year period is considered to be the average length of an economic cycle.

As shown in the following pie charts, diversification means achieving geographical distribution of assets as well as diversifying across different asset classes. Canada accounts for only 3% of the world equity market. The *Federal Income Tax Act* restricts pension funds from investing more than 20% of the book value of the fund outside of the country. However, we have made the most of the allowed 20%, diversifying our equity holdings across the major economies of the world.

### Global Distribution
(Total $2,183.5 million)




### Foreign Equity Distribution
(Total $431.3 million)




## Investment Performance

### General

The Board regularly reviews the fund investment portfolio and measures investment results against external benchmarks. Benchmarks for measuring investment performance are market indices developed and maintained by exchanges, dealers and consultants. The indices we use are widely accepted in the industry and are consistently constructed from year to year. Each index measures the total return (income plus capital gain) achieved by the type of investment it represents.

## Investment Performance (continued)

Fund performance is compared to these external benchmark indices on a time-weighted basis. The time-weighted returns of the fund's investments are calculated by taking into consideration the timing and impact of cash flows. The market indices do not include any transaction fees.

The fund experienced a zero return in 1994, on a market value basis. All funds were affected by poor performance in both bond and equity markets. The median loss among other balanced fund managers was 0.7%. Over a four-year period, the fund achieved a 10.6% return as compared to a median of 11.2%.

The following table provides a summary of the returns achieved for each major asset class over the latest one and four-year periods:

### Comparison of Rates of Return

| (%) | 4 Years | 1 Year |
|---|---|---|
| Cash & short-term securities | 8.2 | 5.2 |
| ScotiaMcLeod 91-day T-bill Index | 6.9 | 5.4 |
| Bonds | 10.9 | -2.5 |
| ScotiaMcLeod Bond Universe Index | 10.9 | -4.3 |
| Mortgages | 8.7 | -2.7 |
| ScotiaMcLeod Bond Universe Index | 10.9 | -4.3 |
| Canadian equities | 8.0 | 1.7 |
| TSE 300 Index | 9.9 | -0.2 |
| Foreign equities | 16.8 | 3.0 |
| Morgan Stanley World Index | 12.8 | 9.6 |
| Real estate | -4.3 | 3.1 |
| Frank Russell Canadian Property Index | -2.6 | 1.7 |
| Total portfolio | 10.6 | 0.0 |
| SEI Balanced Fund Median | 11.2 | -0.7 |
| Inflation Rate | 2.0 | 0.2 |

NOTE: The four-year return includes a period of two years and nine months when the investments were held by the old Pension Fund.

Despite monetary tightening by United States' authorities and the rising trend in interest rates, in general the Canadian and global economies continued to grow in 1994. Real growth in Canada was 4.2%, while the United States, Japan and Germany increased 4.0%, 2.0% and 2.5% respectively. As a result, earnings in Canadian companies rebounded dramatically from their deep recession lows.

### Cash and Short-Term Securities

At the end of 1994, cash and short-term securities totalled $223.7 million, down from the $245.5 million held at the end of 1993. Cash and short-term securities outperformed both domestic bonds and equities during 1994. The achieved four-year rate of return of 8.2% considerably exceeded the ScotiaMcLeod 91-day T-bill Index.

### Bonds

The world-wide bond market was weak in 1994 as pre-emptive monetary tightening by the U.S. Federal Reserve resulted in significantly increased interest rates. Canadian short rates rose 295 basis points while long term rates increased 196 basis points. The yield spread between Canadian and U.S. short rates widened from 85 to 177 basis points while at the long end the spread between Canadian and U.S. government bonds widened from 99 to 129 basis points.

The Plan primarily invests in publicly traded bonds, but some bonds are purchased privately. Bond holdings are diversified and include those issued by the federal government and its agencies as well as provincial governments and corporations.

The performance of the bond segment of the investment portfolio has been consistent with the ScotiaMcLeod Bond Universe Index over the four-year period.

## Investment Performance (continued)

### Mortgages

The fund's mortgage portfolio is relatively small. Despite attracting higher yields than bonds, mortgage returns have been depressed by a weak real estate market that has seen increased mortgage defaults.

### Canadian Equities

The bulk of the fund's Canadian equity portfolio is managed directly by IMD. The holdings are broadly diversified across the major industry sectors of the economy. Most have been acquired through public markets although some have been purchased privately.

During 1994, smaller companies experienced a stronger correction from extremely buoyant performance in 1993. The TSE 35, composed of the 35 largest companies on the Toronto Stock Exchange, produced a total return of 5.5%, while the TSE 300 generated a negative return of 0.2%.

The fund's focus on large capitalization companies and lesser exposure to small capitalization companies enabled us to realize a one-year return of 1.7% which was much higher than the TSE 300 index.

### Foreign Equities

During 1994, world capital markets provided favourable investment results when combined with the depreciation of the Canadian dollar.

Over the last year, the foreign segment of the fund's investment portfolio did not perform as well as its benchmark index, due to a significant under-weighting in Japan by our external managers. Japan is a major component of the benchmark index and until 1994 had lagged the performance of the total index. Although its economic growth was not significant in 1994, Japan managed to stage a technical recovery and exceeded the performance of the total index.

### Real Estate

The real estate market has decreased significantly over the last four years. Accordingly, we have been reducing the fund's exposure to real estate; it currently represents only 2.5% of the fund on a market value basis.

S.J. Susinski
Chief Investment Officer

# PLAN ADMINISTRATION

## Introduction

The administration of the Public Service Pension Plan is carried out by Alberta Pensions Administration (APA), a division of Alberta Treasury. Costs of administration for 1994 amounted to $3,050,000 or $49 per member. The cost per member, excluding investment costs, is $44. Further details relating to administration costs are given in note 6 on page 26 of this report.

A major focus for APA during 1994 was the reprogramming of computer systems to accommodate the changes brought about by pension reform. Significant changes were implemented in June to revise the system of processing applications to purchase prior service, and in September to enable the processing of termination benefits calculated on a commuted value basis. Other pension reform changes are currently being handled through manual procedures and are scheduled to be automated during 1995.

A Board secretariat was established early in 1994 to provide services to the newly appointed Board. APA was heavily involved in developing procedures and documentation relating to Board agendas, the recording and distribution of minutes, and the preparation of information and materials for Board meetings.

APA is committed to providing a quality and cost efficient administration. To assist in meeting this objective, a new system of activity based program budgeting was implemented to enhance understanding and control of costs. In addition, APA has become a participant in a cost comparison survey with other pension plans across Canada.

## Participation

At December 31, 1994 there were 46 employers participating in the Public Service Pension Plan. Membership was made up as follows:

| | 1994 | 1993 |
|---|---|---|
| Active members | 44,981 | 47,882 |
| Inactive members | 2,642 | 2,713 |
| Pensioners | 13,303 | 12,581 |
| TOTAL | 60,926 | 63,176 |

## Contributions

The contribution rates in effect at December 31, 1994 and 1993 were as follows:

| | 1994 % | 1993 % |
|---|---|---|
| Current Service (post-1991) | | |
| Employer and Employee | | |
| Up to YMPE * | 9.35 | 9.150 |
| Above YMPE | 13.10 | 12.900 |
| Unfunded Liability (pre-1992) | | |
| Employer and Employee | 0.60 | 0.400 |
| Province of Alberta | 1.00 | 0.666 |
| TOTAL | | |
| Up to YMPE | 10.95 | 10.216 |
| Above YMPE | 14.70 | 13.966 |

* Yearly maximum pensionable earnings under the Canada Pension Plan.

## Terminations

During 1994, termination benefits of $40,479,000 were paid. Of this amount, $7,878,000 was paid under the terms of various reciprocal agreements. In addition, $32,601,000 was paid to members directly, or transferred to registered retirement savings plans (RRSPs) and locked in retirement accounts. These payments were based on contributions plus interest or the commuted value of service, depending on whether service was pre-1992 or post-1991.

## Pensions

Pension benefits paid totalled $115,472,000 in 1994. During the year a total of 1,037 new pensions were granted in the categories shown below:

| | Number of Pensions | % |
|---|---|---|
| Normal retirements | 131 | 12.6 |
| Early retirements | 857 | 82.6 |
| Disability retirements | 14 | 1.4 |
| Death-in-service (spousal) retirements | 35 | 3.4 |
| | 1,037 | 100.0 |

Of these pensions, 432 were co-ordinated with the Canada Pension Plan and/or federal Old Age Security.

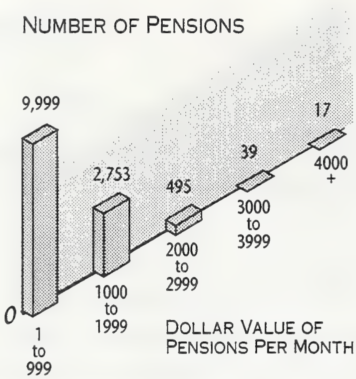
Options chosen in respect of the new retirements were as follows:

| | Number of Options | % |
|---|---|---|
| Single life | 100 | 9.7 |
| Joint life | 608 | 58.6 |
| Guaranteed term | 329 | 31.7 |
| | 1,037 | 100.0 |

As at December 31, 1994 there were a total of 13,303 individual pensions being paid. The schedule and graph below categorize these pensions in terms of the monthly dollar amount being paid:

| Dollar Value Per Month | Member Pensions | Spousal Pensions | Total |
|---|---|---|---|
| 1 to 999 | 9,163 | 836 | 9,999 |
| 1,000 to 1,999 | 2,639 | 114 | 2,753 |
| 2,000 to 2,999 | 490 | 5 | 495 |
| 3,000 to 3,999 | 38 | 1 | 39 |
| 4,000 and over | 16 | 1 | 17 |
| | 12,346 | 957 | 13,303 |

## Pensions (continued)




Effective January 1, 1994, a cost of living adjustment of 0.84% was granted to those pensioners who had been in receipt of a pension for one year or more, with a proportionately smaller increase to those retiring during calendar year 1994. The adjustment was equal to 60% of the increase in the Alberta cost-of-living index.

## Information And Counselling

APA provides information to members and participating employers on all aspects of pension benefits and Plan administration. During 1994, pre-retirement seminars were presented to a total of 1,959 employees, and 15 employer workshops were conducted.

Two pension update information leaflets were provided to employers on the subjects of pension reform and combined pensionable service. Pension information brochures were prepared and made available to members on subjects such as understanding pension estimates, division of pensions on marriage breakdown, and the purchasing of prior service. A new and completely re-written member handbook was produced and distributed to members in November.

A newsletter called *Pension News* was designed to assist employers in keeping abreast of the latest developments relating to their Plan. Three issues of *Pension News* were produced and distributed during the year.

Annual statements containing information on pensionable service, contributions, and prior service were produced and forwarded to employers for distribution to active members.

Annual Reports of the Pension Plan were finalized and tabled in the legislature for the year to March 31, 1993 and the nine months to December 31, 1993. The inaugural financial statements of the Public Service Pension Plan for the three months ending December 31, 1993 were finalized and audited by the Office of the Auditor General.

The Alberta Retired Public Employees Society was again assisted by APA with the production of their quarterly newspaper, *Postscript*.

## Conclusion

Current year results will form the basis for activity in the year ahead as APA focuses on new ways to improve service, while striving to maintain the high productivity levels achieved in 1994.

M.H. Mylod
M.H. Mylod
Director

# ACTUARIAL COST CERTIFICATE

## Buck Consultants

I have performed an actuarial valuation of the Public Service Pension Plan at December 31, 1993. The purpose of this actuarial valuation was to determine the funded status of the Plan at that date and to determine the level of funding required for 1994 and 1995.

The unfunded liability in the Plan has decreased from $681 million in 1991 to $521 million on the valuation date. The unfunded liability has decreased because of the additional contributions made by members of the Plan, their employers and the government in 1992 and 1993. In addition, the experience of the Plan in 1992 and 1993 was favourable. Finally, the actuarial assumptions used to determine the unfunded liability were modified to reflect higher rates of return on the assets expected from the investment policy being developed and implemented by the Board.

The unfunded liability is being funded by additional contributions of 1% of salary by the government and 0.3% by Plan members and their employers. Our actuarial valuation determined that this level of funding is sufficient to eliminate the unfunded liability by the year 2036.

The current service contributions payable by active plan members and their employers with effect from August 1994 were 4.675% of pensionable earnings up to the earnings base of the Canada Pension Plan and 6.55% of earnings in excess of that level. We confirmed that this level of contributions is adequate to fund the cost of benefits accruing to active plan members in 1994 and 1995.

We have recommended that the Board ratify the continuation of the existing level of contributions from members, employers and the government until the next actuarial valuation is performed.

We have certified to the Board in our actuarial report that the plan member data and asset data used in our actuarial valuation was sufficient and reliable and that the assumptions we used were, in the aggregate, appropriate. Our actuarial valuation was performed in accordance with the Standard of Practice for Valuation of Pension Plans issued by the Council of the Canadian Institute of Actuaries. Nevertheless, an actuarial valuation is an assessment of the probable impact of uncertain future events. The actual experience of the Plan will be different from the estimates made at the time of an actuarial valuation. These experience variations will produce either gains or losses, which will be recognized in future actuarial valuations, and the plan funding must be adjusted accordingly in order to ensure that plan benefits will be fully funded.

Our actuarial valuation fully reflected the impact of the reduction in plan membership caused by downsizing in the Alberta public service. In particular, our valuation determined that the contribution level previously established to finance the unfunded liability will remain adequate after all expected downsizing in the Alberta public service is completed. To provide further assurance, we have recommended the establishment of a contingency reserve in the Plan of $58 million. If this reserve is not needed to augment funding caused by downsizing, it may, at the discretion of the Board, be used to provide additional cost-of-living benefits as provided in the pension plan legislation.

William T. Moore, F.S.A., F.C.I.A.
Fellow of the Canadian Institute of Actuaries
March 31, 1995

ALBERTA LEGISLATURE
OFFICE OF THE AUDITOR GENERAL

## AUDITOR'S REPORT

To the Public Service Pension Board
and the Provincial Treasurer

I have audited the statement of net assets available for benefits and accrued pension benefits of the Public Service Pension Plan as at December 31, 1994 and the statements of changes in net assets available for benefits and accrued pension benefits for the year then ended. These financial statements are the responsibility of the Plan's management. My responsibility is to express an opinion on these financial statements based on my audit.

I conducted my audit in accordance with generally accepted auditing standards. Those standards require that I plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In my opinion, these financial statements present fairly, in all material respects, the financial position of the Plan as at December 31, 1994 and the results of its operations and the changes in its financial position for the year then ended in accordance with generally accepted accounting principles.

Peter Valentine

FCA
Auditor General

Edmonton, Alberta
May 3, 1995

# FINANCIAL STATEMENTS

## STATEMENT OF NET ASSETS AVAILABLE FOR BENEFITS AND ACCRUED PENSION BENEFITS

AS AT DECEMBER 31, 1994
($ THOUSANDS)

| | 1994 | 1993 |
|---|---|---|
| NET ASSETS AVAILABLE FOR BENEFITS | | |
| **Assets** | | |
| Investments (Note 3) | 2,183,469 | 2,198,932 |
| Accounts receivable (Note 4) | 41,745 | 33,085 |
| | 2,225,214 | 2,232,017 |
| **Liabilities** | | |
| Accounts payable | 12,791 | 5,016 |
| **Net assets available for benefits** | 2,212,423 | 2,227,001 |
| Actuarial asset value adjustment (Note 7) | 62,866 | 180,016 |
| **Actuarial value of net assets available for benefits** | 2,149,557 | 2,046,985 |
| ACCRUED PENSION BENEFITS | | |
| **Accrued pension benefits (Note 7)** | 2,768,000 | 2,568,000 |
| **Deficiency of actuarial value of net assets over accrued pension benefits (Note 7)** | 618,443 | 521,015 |

See accompanying notes.

## STATEMENT OF CHANGES IN NET ASSETS AVAILABLE FOR BENEFITS

YEAR ENDED DECEMBER 31, 1994
($ THOUSANDS)

| | 1994 | Three Months Ended December 31, 1993 |
|---|---|---|
| **Increase in assets** | | |
| Investment (loss) income (Note 5) | (13,310) | 111,149 |
| Interest on Province of Alberta receivable (Note 4) | 627 | 156 |
| Contributions | | |
| Current and past service | | |
| Employers | 66,564 | 17,942 |
| Employees | 70,321 | 18,890 |
| Pre-1992 Unfunded liability | | |
| Employers | 3,545 | 787 |
| Employees | 3,545 | 787 |
| Province of Alberta | 11,818 | 2,625 |
| Transfers from other plans | 1,313 | 470 |
| | 157,106 | 41,501 |
| Total increase in assets | 144,423 | 152,806 |
| **Decrease in assets** | | |
| Benefits | 115,472 | 28,100 |
| Refunds to members | 32,601 | 4,525 |
| Transfers to other plans | 7,878 | 1,353 |
| Administration expenses (Note 6) | 3,050 | 814 |
| Total decrease in assets | 159,001 | 34,792 |
| **Increase (decrease) in net assets for the period before transfers** | (14,578) | 118,014 |
| Transfers from the Province of Alberta | | |
| Pension Fund | – | 2,101,347 |
| General Revenue Fund | – | 7,640 |
| | – | 2,108,987 |
| **Change in net assets for the period** | (14,578) | 2,227,001 |
| **Net assets available for benefits at beginning of period** | 2,227,001 | – |
| **Net assets available for benefits at end of period** | 2,212,423 | 2,227,001 |

See accompanying notes.

## STATEMENT OF CHANGES IN ACCRUED PENSION BENEFITS

FOR THE YEAR ENDED DECEMBER 31, 1994
($ THOUSANDS)

| | Year Ended December 31, 1994 | | | Two Years Ended December 31, 1993 |
|---|---|---|---|---|
| | Pre-1992 | Post-1991 | Total | Total |
| **Increase in Accrued Pension Benefits** | | | | |
| Interest accrued on benefits | 202,000 | 28,000 | 230,000 | 421,000 |
| Benefits earned | – | 110,000 | 110,000 | 249,000 |
| | 202,000 | 138,000 | 340,000 | 670,000 |
| **Decrease in Accrued Pension Benefits** | | | | |
| Benefits paid | 130,000 | 10,000 | 140,000 | 259,000 |
| Net experience gains | – | – | – | 13,000 |
| Changes in actuarial assumptions (Note 7) | – | – | – | 206,000 |
| | 130,000 | 10,000 | 140,000 | 478,000 |
| **Net increase in accrued pension benefits** | 72,000 | 128,000 | 200,000 | 192,000 |
| **Accrued pension benefits, beginning of period** | 2,309,000 | 259,000 | 2,568,000 | 2,376,000 |
| **Accrued pension benefits, end of period** | 2,381,000 | 387,000 | 2,768,000 | 2,568,000 |

See accompanying notes.

# NOTES TO THE FINANCIAL STATEMENTS

DECEMBER 31, 1994

## Note 1 Summary Description of the Plan

The following description of the Public Service Pension Plan is a summary only. For a complete description of the Plan, reference should be made to the Public Sector Pension Plans Act, Chapter P-30.7, Statutes of Alberta 1993, and Alberta Regulation 368/93.

### (a) General

The Public Service Pension Plan is a contributory defined benefit pension plan for eligible employees of the Province of Alberta, approved provincial agencies and public bodies, including universities and local boards of health units established under the Public Health Act and the Special Areas Board.

### (b) Funding

Current service costs are funded equally by employers and employees at rates which are expected to provide for all benefits payable under the Plan. The rates in effect are 4.675 percent of pensionable salary up to the Canada Pension Plan's Year's Maximum Pensionable Earnings (YMPE) and 6.55 percent for the excess. The rates are to be reviewed at least once every three years by the Board based on recommendations of the Plan's actuary.

The unfunded liability for service prior to December 31, 1991 as determined by actuarial valuation is being financed by additional contributions in the ratio of 62.5 percent by the Province of Alberta, and 18.75 percent each by employers and employees. The rates are set on the basis that the additional contributions will eliminate the unfunded liability on or before December 31, 2036. The rates in effect, based on pensionable salary, are 1.0 percent for the Province of Alberta, and 0.30 percent each for employers and employees.

### (c) Retirement Benefits

The Plan provides for a pension of 1.4 percent of the highest five year average salary up to the YMPE, and 2 percent of the excess for each year of pensionable service. The maximum pensionable service allowable under the Plan is 35 years. Pensions are payable to members who retire with at least five years of service, and either have attained age 65, or have attained age 55 and the sum of their age and years of service equals 85. Reduced pensions are payable to members age 55 retiring early with a minimum of five years service.

### (d) Disability Benefits

Pensions are payable to members who become totally disabled and retire early with at least five years of service. Reduced pensions are payable to members who become partially disabled and retire early with at least five years of service.

## Note 1 Summary Description of the Plan (continued)

**(e) Death Benefits**

Death benefits are payable on the death of a member. If the member has at least five years service, a surviving spouse may choose to receive a survivor pension. For a beneficiary other than a spouse, or where service is less than five years, a lump sum payment must be chosen.

**(f) Termination Benefits**

Members who terminate with at least five years of service, and are not immediately entitled to a pension, may receive a refund of contributions and interest on service prior to 1992, and the commuted value for service after 1991, subject to lock-in provisions. Alternatively, they may elect to receive a deferred pension. Members who terminate with less than five years of service receive a refund of their contributions and interest.

**(g) Prior Service and Transfers**

All prior service purchases are to be made on a basis that is cost neutral to the Plan.

During 1994, transfers under the terms of reciprocal agreements were costed according to the Plan's requirements for employee and employer contributions plus interest. All reciprocal agreements must be renegotiated to provide that transferred-in service be on a cost neutral basis, and transfers-out receive the greater of the termination benefits or commuted value for all service.

**(h) Cost-of-Living Adjustments**

Pensions payable are increased each year by an amount equal to at least 60 percent of the increase in the Alberta Consumer Price Index.

**(i) Income Taxes**

The Plan is a registered pension plan as defined in the Income Tax Act, and is not subject to income taxes. The Plan's registration number is 0208769.

## Note 2 Summary of Significant Accounting Policies and Reporting Practices

**(a) Basis of Presentation**

These financial statements are prepared on the going concern basis in accordance with generally accepted accounting principles. The statements provide information about the net assets available in the Plan to meet future benefit payments, and are prepared to assist plan members and others in reviewing the activities of the Plan for the year. They do not reflect the funding requirements of the Plan or the benefit security of individual participants.

## Note 2 Summary of Significant Accounting Policies and Reporting Practices (continued)

The majority of plan investments are held in pooled investment funds established and administered by the Provincial Treasurer. Pooled investment funds have a market based unit value that is used to allocate income to participants and to value purchases and sales of pool units. The net investment loss derived from pooled funds during 1994 was $33.8 million (1993: income of $108.3 million for three months) and the net assets at December 31, 1994 were $1.6 billion (1993: $2.1 billion).

Included in these financial statements are the accounts of the Plan and the Plan's proportionate share of the assets, liabilities and net income of the pooled funds shown below with their respective percentage ownership at December 31, 1994:

| | % |
|---|---|
| Canadian Dollar Public Debt Pool | 20.0 |
| Canadian Pooled Equities Fund | 0.0 |
| External Managers Fund | 17.5 |
| Money Market Pool | 0.0 |
| Private Debt Pool | 18.6 |
| Private Equity Pool | 17.0 |
| Private Mortgage Pool | 17.0 |
| Private Real Estate Pool | 19.0 |
| United States Pooled Equities Fund | 20.5 |

### (b) Valuation of Investments

Investments are stated at market value. The methods used to determine market value are explained in the following paragraphs.

Short-term securities, public fixed interest bonds, foreign equities and Canadian equities are valued at the year end closing sale price, or the average of the latest bid and ask prices quoted by an independent securities valuation company.

Private fixed interest bonds and mortgages are valued based on the net present value of future cash flows. These cash flows are discounted using Government of Canada bond rates adjusted for a risk premium estimated by management.

The market value of private equities is estimated by management.

Real estate investments are reported at their most recent appraised value, net of any liabilities against the real property. Real estate properties are appraised at least triennially by qualified external real estate appraisers.

Purchases and sales of investments are recorded on the dates traded.

## Note 2 Summary of Significant Accounting Policies and Reporting Practices (continued)

c) **Income Recognition**

Dividends are accrued on the ex-dividend date. Income from other investments is accrued as earned. Gains or losses on investments are recognized concurrently with changes in market value.

d) **Foreign Exchange**

Foreign currency transactions are translated into Canadian dollars using average rates of exchange, except for hedged foreign currency transactions which are translated at rates of exchange established by the terms of the forward exchange contracts. At the year end, the market value of investments and any other assets and liabilities denominated in a foreign currency are translated at the year end exchange rate. Exchange differences are included in the determination of investment income.

## Note 3 Investments

Investments are summarized as follows:

| | 1994 | 1993 |
|---|---|---|
| | ($ THOUSANDS) | |
| Cash and short-term securities | 223,676 | 245,467 |
| Bonds | 909,181 | 937,955 |
| Mortgages | 64,002 | 69,530 |
| Canadian equities | 500,058 | 448,805 |
| Foreign equities | 431,271 | 443,427 |
| Real estate | 55,281 | 53,748 |
| | 2,183,469 | 2,198,932 |

The above amounts include $67,809,000 (1993: $102,097,000) of investments issued by the Province of Alberta.

Real estate is held through intermediate companies which have issued common shares and participating debentures secured by a charge on real estate. The rental income less expenses and other adjustments is distributed to the Plan through the Private Mortgage and Private Real Estate Pools.

Intermediate companies which are owned 20 percent or more by the Private Real Estate Pool are as follows:

| | % OWNERSHIP | |
|---|---|---|
| | 1994 | 1993 |
| ARCA Investments Inc. | 100.0 | 100.0 |
| ORION Properties Ltd. | 100.0 | 100.0 |
| RT 10th Pension Properties Ltd. | 100.0 | - |
| RT 7th Pension Properties Ltd. | 71.4 | 71.4 |
| RT Pension Properties Ltd. | 67.7 | 67.7 |
| RT 8th Pension Properties Ltd. | 33.3 | 33.3 |
| 629851 Ontario Inc. | 27.9 | 27.9 |

## Note 4 Accounts Receivable

| | 1994 | 1993 |
|---|---|---|
| | ($ thousands) | |
| Receivable from sale of investments and accrued investment income | 22,043 | 20,114 |
| Contributions receivable | | |
| Employers | 5,390 | 2,232 |
| Employees | 5,581 | 2,224 |
| Province of Alberta | 1,256 | 875 |
| Receivable from Province of Alberta | 7,475 | 7,640 |
| | 41,745 | 33,085 |

The amount due from the Province of Alberta is the Plan's share of the accumulated excess of benefits over contributions paid to Members of the Legislative Assembly prior to October 1, 1993. The amount due attracts interest at 8.09 percent and is scheduled to be repaid in annual instalments ending September 30, 2013. The Province may repay the whole or any part of the debt at any time.

## Note 5 Investment Income

| | 1994 | | | Three Months Ended December 31, 1993 |
|---|---|---|---|---|
| | Income | Change in Market Value | Total | Total |
| | ($ thousands) | | | |
| Cash and short-term securities | 11,423 | (5,878) | 5,545 | 4,116 |
| Bond | 71,523 | (106,991) | (35,468) | 48,897 |
| Mortgages | 6,656 | (8,089) | (1,433) | 2,593 |
| Canadian equities | 13,372 | (9,517) | 3,855 | 39,507 |
| Foreign equities | 26,704 | (13,792) | 12,912 | 21,331 |
| Real estate | 3,097 | (1,818) | 1,279 | (5,295) |
| | 132,775 | (146,085) | (13,310) | 111,149 |

Of the above amounts, $7,625,000 of income and ($10,123,000) of the change in market value is derived from investments issued by the Province of Alberta.

Income is comprised of dividends, interest, rental income and other non-capital returns from assets. Current period change in market value represents the change in market value of investments during the year.

## Note 6 Administration Expenses

| | 1994 | Three Months Ended December 31, 1993 |
|---|---|---|
| | ($ thousands) | |
| Plan administration costs | 2,597 | 759 |
| Investment management costs | 315 | 55 |
| Professional fees | 125 | – |
| Board costs | 13 | – |
| | 3,050 | 814 |

The above investment management costs are those charged on a cost recovery basis directly by Alberta Treasury, and do not include custodial and external management fees which have been deducted in arriving at investment income. Board costs include travel and related expenses incurred by Board members.

In 1994, total administration costs of $3,050,000 amounted to $49 per member.

## Note 7 Accrued Pension Benefits

An actuarial valuation of the Plan was carried out as at December 31, 1993 by Buck Consultants Limited, and was then extrapolated to December 31, 1994. The December 31, 1993 valuation resulted in an actuarial deficiency of $521 million as disclosed in the statement of accrued pension benefits and net assets available for benefits. The previously reported unfunded liability of $744 million at December 31, 1993 was based on a valuation carried out as at December 31, 1991, which was then extrapolated to December 31, 1993. The decrease in the December 31, 1993 actuarial deficiency resulted from changes in assumptions and experience gains during the two-year period.

## Note 7 Accrued Pension Benefits (continued)

The valuation as at December 31, 1993 was determined using the projected benefit method, prorated on service. The assumptions used in the valuation were developed by reference to management's best estimate of expected short and long-term economic conditions. The major assumptions used were:

| | | December 31 | |
|---|---|---|---|
| | 1994 Extrapolation % | 1993 Valuation % | 1991 Valuation % |
| Asset real rate of return | 4 | 4 | 3.5 |
| Inflation rate | 5 | 5 | 5 |
| Salary escalation rate | | | |
| until 1997 | 4.2 to 6 | 4.2 to 6 | 2 to 5 |
| thereafter | 6 | 6 | 5 |
| Pension cost of living increase as a percent of Alberta Consumer Price Index | 60 | 60 | 60 |

In accordance with the requirements of the Public Sector Pension Plans Act, a separate accounting is required of the pension liability with respect to service that was recognized as pensionable as at December 31, 1991. This information is provided in the statement of changes in accrued pension benefits which shows the principal components of the change in the actuarial value of accrued pension benefits between the last two actuarial valuations, and as extrapolated to December 31, 1994.

Investments held by the Plan are valued at market value at December 31, 1994 for financial statement purposes. However, in order to moderate the effects of market volatility on investment values, the actuarial value of assets has been determined by averaging market values over the three year period ended December 31, 1994. As with the accrued pension benefits, the assets have been split between the pre-1992 and post-1991 periods.

## Note 7 Accrued Pension Benefits (continued)

The following table summarizes the actuarial value of net assets, accrued benefits, and the resulting actuarial deficiency at December 31, 1994.

| | PRE-1992 | POST-1991 ($ THOUSANDS) | TOTAL |
|---|---|---|---|
| Market value of net assets | 1,757,160 | 455,263 | 2,212,423 |
| Actuarial asset value adjustment | 57,913 | 4,953 | 62,866 |
| Actuarial value of net assets | 1,699,247 | 450,310 | 2,149,557 |
| Accrued pension benefits | 2,381,000 | 387,000 | 2,768,000 |
| Actuarial deficiency (surplus) | 681,753 | (63,310) | 618,443 |

The actuarial surplus related to pensionable service performed after 1992 of $63,310,000 is being held as a reserve for future benefit enhancement on the recommendation of the Plan's actuary.

## Note 8 Comparative Figures

Comparative figures have been restated to be consistent with the 1994 presentation and to recognize the results of the 1993 actuarial valuation.

On September 30, 1993 certain sections of the Public Sector Pension Plans Act came into force which established the Public Service Pension Plan Fund and transferred the Plan's share of the Pension Fund as at September 30, 1993 into the Public Service Pension Plan Fund. Accordingly, the comparative figures for the statement of changes in net assets available for benefits are for the three month period ending December 31, 1993.

The Comparative figures for the statement of changes in accrued pension benefits are for the two years ended December 31, 1993 to reflect the change in accrued pension benefits from the previous valuation carried out as at December 31, 1991.

## Note 9 Responsibility for Financial Statements

These financial statements were approved by the Public Service Pension Board.

## Mission Statement of the Public Service Pension Board

"The Board will act solely in the interest of plan stakeholders to ensure that:

- contributions are invested prudently
- the Plan is managed effectively and efficiently and is operated in compliance with legislation and regulations.

In fulfilling its mission, the Board will consider the:

- overall financial health of the Plan
- future development of plan provisions
- costs of the Plan
- stakeholders' concerns and information needs."